The Economic Impact of China and India on Southeast Asia

Manu Bhaskaran

Introduction

China's growing economic clout is increasingly felt in Southeast Asia. Competition has intensified in trade and foreign direct investment (FDI). Many companies in the region are finding it hard to compete against the lower prices offered by Chinese competitors. At the same time, China's voracious appetite for imports and the growing numbers of Chinese tourists have also brought good news. Just as the region is adjusting to China's growing economic presence, it is also now evident that India is also casting a potentially competitive shadow over Southeast Asian economies — it is beginning to attract more FDI and it is clearly highly competitive in several service activities.

This chapter will argue that the emergence of China and India will precipitate substantial policy and micro-level changes to the region. These adjustments will help Southeast Asian economies to respond to the growing competition and so permit them to find their own niches in the emerging new division of labour. In the process, there will be many winners and quite a few losers in the region. Whether the balance is a net positive or a net negative will depend on how effectively each country adjusts to the more competitive world that China and India create. It is argued here that the winners will be those countries that have the political will to reinvent policies and the entrepreneurial capacity to adapt and re-engineer the microeconomy.

This chapter will begin with a review of how China and India have affected the regional economies in trade, investment and other economic areas. It will then review how these countries are adjusting to this new world and conclude with an assessment of what the net impact would be on economic growth and development in the region.

MANU BHASKARAN is Partner, Centennial Group and Adjunct Senior Research Fellow, Institute of Policy Studies, Singapore.

Recent Economic Trends

Goods Trade: China's Increased Share of Exports not at Region's Expense

Recent trends in global exports of merchandise goods and of services are presented in Figures 1 and 2 and Table 1. A number of important features stand out:

- Both China and Southeast Asia increased their share of global merchandise exports in 1990–2002. China's increased share did not come at the expense of Southeast Asia in general. India's share has increased much more slowly in trade. Southeast Asia has seen its share of global merchandise exports slip a little from the peak it reached in the mid-1990s but generally has clung on to its global export position.

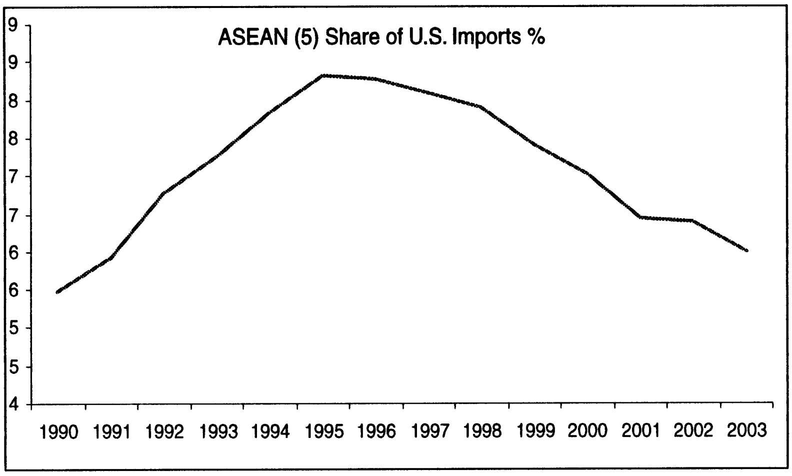
Given that India's goods exports have not really posed a challenge to Southeast Asia yet, we will focus on China's impact:

- It is also noteworthy (see Figure 3) that China has increased its share of U.S. imports while many Southeast Asian economies have seen their share of the U.S. market diminish.

FIGURE 1
China, ASEAN, raised share of merchandise exports

Source: Collated by Centennial Group using CEIC Database and World Trade Organization (WTO) data.

FIGURE 2
Southeast Asian share of U.S. market fell ...



Source: Collated by Centennial Group using CEIC Database and WTO data.

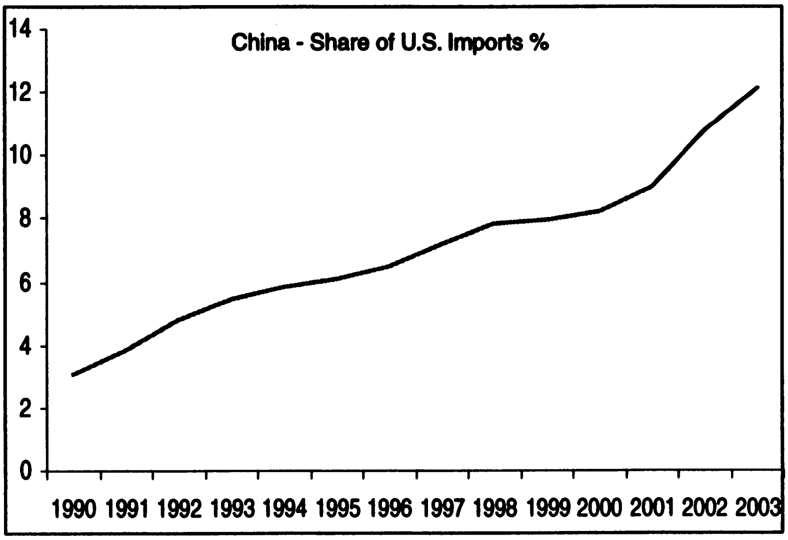
TABLE 1
Shares of global merchandise exports by country

	1990	1995	2003
China	1.5	2.5	5.8
India	0.5	0.6	0.8
ASEAN-5	3.3	6.1	5.9
Indonesia	0.8	0.9	0.8
Malaysia	1	1.4	1.4
Philippines	0.2	0.3	0.5
Singapore	1.6	2.4	2.1
Thailand	0.7	1.1	1.0

Source: Collated by Centennial Group using WTO data.

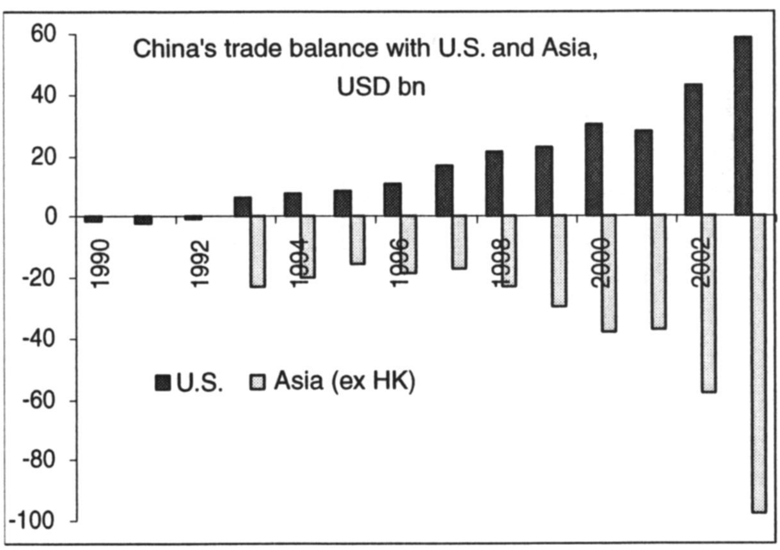
- China's goods imports from Southeast Asia have grown rapidly, in fact with extraordinary strength. As a result, China has seen its trade deficit with Southeast Asia grow rapidly. As Figure 4 shows, the growth of this trade deficit mirrors the expansion of China's trade surplus with the United States.
- At the same time, it is also important to note that Southeast Asian exports to China have grown rapidly (see Figure 5).

FIGURE 3
China's share of U.S. market rose



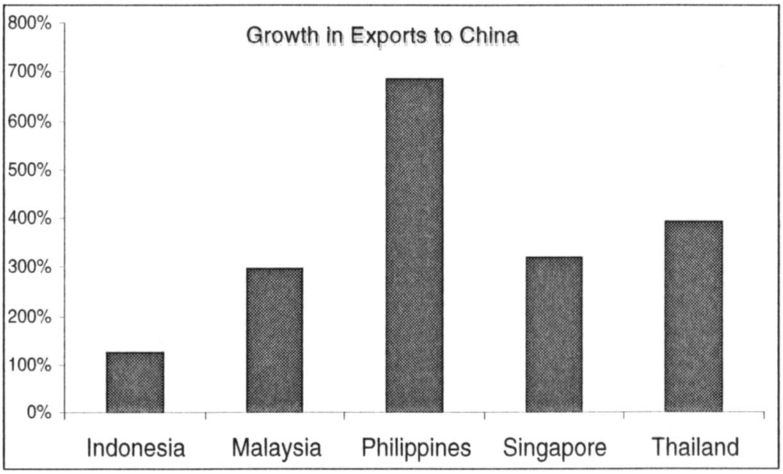
Source: Collated by Centennial Group using CEIC Database and WTO data.

FIGURE 4
China trade surplus with U.S. mirrors deficit with Southeast Asia



Source: Collated by Centennial Group using CEIC Database and WTO data.

FIGURE 5
Southeast Asian exports to China growing rapidly



Note: Cumulative percentage growth in exports of each country to China October 1998 to October 2004.
Sources: Collated by the Centennial Group using CEIC Database.

This brings out a crucial feature of the new division of labour. China is increasingly sourcing raw materials and industrial components from Southeast Asia, among others. Whereas in the past, those industrial components were probably processed within Southeast Asia into finished goods for export to the U.S. market by a Southeast Asian economy, these components are now exported to China where the finished good is assembled and then sent to the U.S. market to be recorded as a Chinese rather than Southeast Asian export. Since the global data suggest that Southeast Asia has gained an increasing share of global exports, this changing division of labour has been a win-win position for both China and Southeast Asia.

Thus, China's rising trade surplus with the United States is a sign of this changing division of labour — where the latter might have imported these goods from a range of Asian economies in the past, these imports in final form tend to now come from China even though much of the intermediate production might have been undertaken in a Southeast Asian (or other) economy. Similarly, the Southeast Asian countries' rising trade surplus with China is not indicative of, say, their currencies being undervalued with respect to the Chinese renminbi (RMB) but of their position in the supply chain.

Services Exports: ASEAN Share Falling

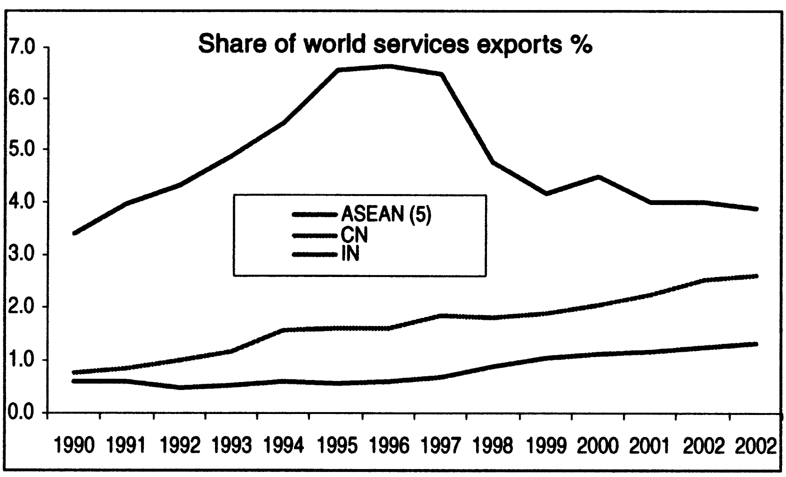
There is clearer evidence that ASEAN appears to be falling behind in the services arena. Figure 6 shows how:

- Southeast Asia's share of global services exports has fallen (Figure 6). However, if we break down the data by country, this fall is almost entirely due to a sharp fall in the share of the Philippines while the shares of Indonesia, Malaysia, Singapore and Thailand have actually crept up somewhat.
- China's share has grown massively even compared to India's, despite the latter's much-vaunted competitive positioning in offshore services and software development.

FDI Trends — No Respite for Southeast Asia as India Revs Up

China has certainly enjoyed a substantial rise in FDI flows. At the same time, Southeast Asia has seen a material fall in FDI flows, except in Singapore. Many have drawn the conclusion that this means that China is gaining in the FDI stakes at the expense of Southeast Asia. However, the true picture might be somewhat more complex.

FIGURE 6
Chinese share of services exports rose, ASEAN fell



Source: Collated by the Centennial Group using CEIC Database.

As Table 2 shows, while China has seen its share of FDI into developing countries rise sharply in the past two years, on average for the period 1998–2003, its share had actually fallen compared to the 1992–97 period. With the opening of Latin America, the former Soviet Union and India, there are simply more economies that are opening up to foreign investment and making a serious effort to woo FDI. It is not just China that is eating into Southeast Asia's share of global FDI flows: many other countries are involved and China too faces competition.

Note also that year-to-year economic developments and exogenous shocks also play an important role in shaping shares of global FDI flows. Just after the Asian financial crisis (1997–98) it was not just Southeast Asia but also China that seems to have lost out in terms of attracting flows of FDI — to the benefit of Latin America. In 2004, although complete data is not yet available, it is also clear that the euphoria surrounding China's economic prospects has caused China's share of global FDI to rise sharply.

Rising Challenges to Southeast Asia

An analysis of the mechanisms at work in global investing point to more challenges for Southeast Asia in coming years.

China to continue drawing disproportionate share of FDI, India will take more FDI

First, global investors can allocate capital across several countries. Originally, Southeast Asia was open and China and India were relatively closed or investment in these latter countries was difficult for a variety of reasons. Thus, up to the mid-1990s, Southeast Asia received a disproportionate share of global FDI. Then, China opened up and progressively cleaned up its regulatory and business environment thereby making FDI into China feasible and increasingly attractive. Not surprisingly, the optimal allocation of capital to China for any given global company increased sharply — and naturally at the expense of those who had had a head start such as Southeast Asia. It is not clear at what point global investors are comfortable with their allocation to China vis-à-vis Southeast Asia and others — that is at which point FDI flows into China and into Southeast Asia will stabilize at a new optimum level. Currently, the stock of FDI in Southeast Asia is still larger than the stock of FDI in China, which is a substantially larger economy. That suggests that we will still see many more years when China attracts sizeably more FDI than Southeast Asia.

Another reason for believing this is China's huge supply side efficiency gains that have boosted the profitability of investing in China in recent years. In addition,

TABLE 2
Share of FDI flows to developing countries including China, India and Southeast Asia
(per cent)

Regions/Countries	1992–97	1998–2003	1998	1999	2000	2001	2002	2003
Africa	5.0	6.4	4.7	5.0	3.5	8.9	7.5	8.7
Latin America/Caribbean	32.2	38.2	42.5	46.3	38.6	40.1	32.6	28.9
Asia-Pacific	62.8	55.4	52.8	48.7	57.9	51.0	59.9	62.4
China	27.7	23.8	23.4	17.4	16.1	21.3	33.5	31.1
Hong Kong	6.6	11.3	7.6	10.6	24.5	10.8	6.1	7.9
India	1.4	1.6	1.4	0.9	0.9	1.5	2.2	2.5
Indonesia	3.0	–0.7	–0.1	–0.8	–1.8	–1.4	0.1	–0.3
Korea	1.1	2.6	2.6	4.1	3.4	1.7	1.9	2.2
Malaysia	4.9	1.4	1.4	1.7	1.5	0.3	2.0	1.4
Philippines	1.1	0.7	1.1	0.7	0.5	0.4	1.1	0.2
Singapore	7.0	5.8	4.0	6.9	6.8	6.8	3.6	6.6
Taiwan	1.2	1.1	0.1	1.3	2.0	1.9	0.9	0.3
Thailand	1.9	1.9	3.9	2.6	1.3	1.7	0.7	1.0
Vietnam	1.3	0.7	0.9	0.6	0.5	0.6	0.8	0.8

Source: Calculated from UNCTAD, *World Investment Report 2004.*

there is also an added layer of high returns on capital as a result of China being in the upside of its economic cycle. Thus, returns on capital invested in China appear to have caught up and overtaken those available in Southeast Asia (Figure 7) — another reason for FDI to flow into China more than into Southeast Asia.

What is more, India is also more likely to draw investments. As Figure 8 shows, its returns on investment have recovered sharply and as Table 3 shows, its attractiveness to global investors has increased sharply in the past three years, as measured by the A.T. Kearney FDI Confidence Index.

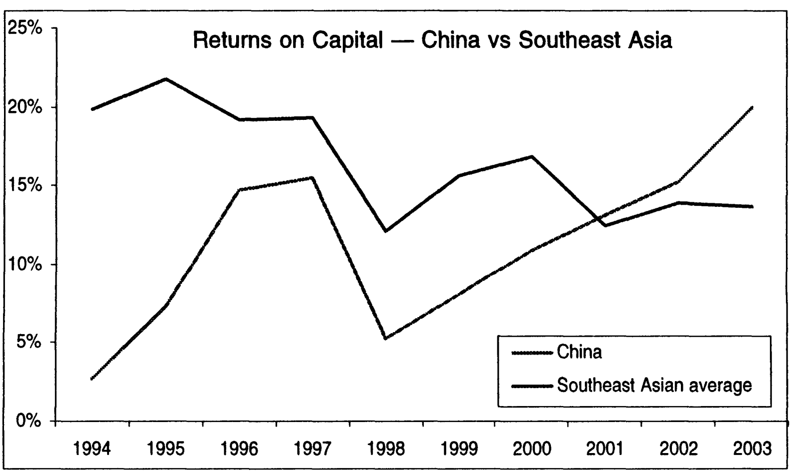
Indian Manufacturing Likely to Become More Competitive

The Indian manufacturing sector is undergoing a significant overhaul, one that is resulting in greater export competitiveness as well as an increased capacity to attract FDI in future.

Efficiency gains from increased competition = greater export competitiveness

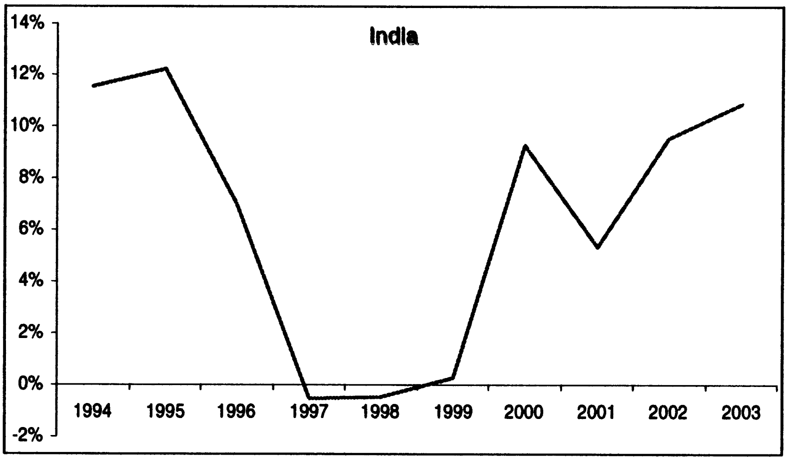
Increased external competition as a result of trade liberalization and intensive domestic competition as a result of excess capacity in the 1990s forced Indian manufacturing companies to undergo several years of restructuring. This period has

FIGURE 7
Returns in China up strongly for Southeast Asia



Source: Collated by the Centennial Group using U.S. Bureau of Economic Analysis data.

FIGURE 8
... while Indian returns have recovered



Source: Collated by the Centennial Group using U.S. Bureau of Economic Analysis data.

TABLE 3
India improves in FDI confidence index

A.T. Kearney Survey Ranking	Rank 2004	Rank 2003	Rank 2002
China	1	1	1
India	3	6	15
Hong Kong	8	22	18
Malaysia	15	23	n.a.
Singapore	18	28	22
Thailand	20	16	20
Indonesia	23	25	n.a.
South Korea	21	18	21
Taiwan	25	20	24

Source: Collated by Centennial Group from various issues of the A.T. Kearney FDI Confidence Index.

produced increasing efficiencies. Take Bajaj Auto as an example: exports are expected to be 15 per cent of sales in FY2004/05 compared with less than 5 per cent in FY2002/03. Bajaj used its tie-up with Kawasaki Heavy Industries to re-tool factories, redesign models and expand its product range to include motorcycles. Similarly, Tata Motors used to make 129,000 cars in 1999 with 35,000 workers. Today it makes more than 300,000 with 40 per cent fewer workers.

The textile industry has also been upgrading itself, having invested US$700m in new mills and equipment in the past two years, and US$2.5bn more to be spent through 2005. Consequently, India is poised to exploit several areas of competitive advantage in this broad sector. For example, the consulting firm McKinsey has found that India retains its edge as the world's largest producer of yarn, with a 25 per cent share of the world market plus also being a leading producer of cotton fibre. It also found that Indian skilled labour enables India to be a more competitive producer of terrycloth and denim than China. India also has strong niche positions in upper-market items where customized weaves, colours and embroideries are desired such as bed sheets, towels and rugs.

This process has now also resulted in increasing export competitiveness. Manufactured goods made up 78 per cent of exports in FY2002/03 compared to 56 per cent 20 years ago.

This increased efficiency is now resulting in global producers relocating more production to India: for example, Toyota opened a factory making gear boxes (only the fourth of its kind in the world) for utility vehicles, which will be assembled in other parts of Asia, South Africa and South America. From 2003, Hyundai shifted its entire global production of the Sentro compact car to India. Unilever India was selected by its parent in May 2003 to produce toothpaste for export to Europe after an internal study showed India to be among the cheapest places to manufacture personal care products. LG Electronics of Korea is to spend US$150m by 2007 to make India its second largest overseas production base after China for consumer electrical and electronics products. India is also making headway in information technology (IT) hardware and related manufacturing. IT hardware exports have jumped from around US$300m in 1999–2000 to US$1bn in 2000–2001 and further to US$2.6bn in 2001–2002.

A More Supportive Policy Environment

Policy changes are lending more support to manufacturing sector growth. India has just established its first Chinese-style Special Economic Zone (SEZ) in Chennai. As in China, locating operations in these SEZs frees companies from onerous labour and tax laws. The government is also stepping up infrastructure spending in addition to the US$177bn infrastructure spending already planned. So far in 2004, 12 new private power plants worth US$2.6bn have been approved, which will add 5,000MW to the power grid (see section on construction below). The government has also announced a new trade policy aimed specifically at increasing India's share of exports from 0.7 per cent to 1.5 per cent. Substantial tax and import duty concessions will be offered to exporters.

Surging Investment in Manufacturing

Indian companies are planning US$105bn in capital spending with investment in automobiles, auto parts, machine engineering, textiles and pharmaceuticals estimated to rise 8.2 per cent in 2004 compared to only 3.6 per cent in 2003. For instance, Tata Steel plans to spend US$3.2bn to expand domestic capacity from 3m tonnes to 7.5m tonnes. Foreign investors are also stepping up their investment in Indian manufacturing:

- POSCO is to invest US$8.4bn over 15 years in steel plant with an annual capacity of 10m tonnes. The first phase of 3m tonnes is to be ready by 2009.
- LG Electronics is to invest US$150m in India by 2007 with investments including a second home appliances plant and a GSM handset production plant. Consequently, LG Electronics will double exports of mobile phone sets and other equipment in 2005 to US$140m.

Increased Innovation Capacity

India is also making some headway in developing its capacity to innovate — a key to achieving higher growth rates. Some examples help to substantiate this point: Intel India filed 63 patents in 2003 alone. The clustering of technology firms and schools in Bangalore is providing India's key IT centre with critical mass. Bangalore now has 140,000 IT professionals, 20,000 more than Silicon Valley. Some 50 colleges there produce about 40,000 IT graduates more each year.

India is rapidly expanding its role in global pharmaceutical production and innovation. Eli Lilly is significantly increasing its research & development (R&D) budget from INR85m in 2002 to INR100m in 2003 and INR110m in 2004. The company is mainly focusing on Phase II–IV work in therapeutic areas of diabetes, oncology, infectious diseases, critical care and women's health. Aventis, which had earlier focused more on Phase II and IV studies in India, is now going for Phase III work as well in therapeutic areas of diabetes, cardiovascular diseases and oncology. ABB, the US$23bn global leader in power and automation technologies, plans to double the headcount at its IT R&D centre in Bangalore. The two-year old company will have 100 employees by the end of 2004, with further additions on the cards for the next two years.

But Indonesia Could Well Reverse its Decline

One major reason for ASEAN's underperformance in attracting FDI has been the ongoing political and economic crisis in Indonesia, which meant that Indonesia's

share of global FDI flows has actually been negative. Not only did its decline hurt the overall figure for all of ASEAN but the travails Indonesia has endured also served to raise investors' perception of risk for all of Southeast Asia — given that Indonesia is the giant in Southeast Asia and that its economic and political difficulties risk spilling over into the rest of ASEAN — especially Singapore, Malaysia and Brunei to which countries Indonesia is geographically and ethnically close.

However, there are now reasons to be more optimistic about Indonesia. A revival in political confidence is now underway following Susilo Bambang Yudhoyuno's election as president. The new administration's policies look likely to improve governance and reduce the risks that foreign investors had faced as a result of corruption in the bureaucracy and judiciary. In addition, there are strong signs that a sustained economic revival is also in process. Data on GDP, capital goods imports and bank lending are all pointing to the strongest growth since the crisis in the next one to two years. Higher growth is likely to raise investors' expectations of returns on capital while improved governance will help reduce the risks associated with such investment. Flows of net FDI are expected to turn positive in 2005 and rise thereafter. The tragic effects of the tsunami that hit Indonesia's northern province of Aceh on 26 December 2004 are not likely to alter this assessment. Aceh as a whole only contributes about 2.7 per cent of Indonesia's GDP — much of this is from the natural gas facilities, which being located away from the tsunami-affected areas, escaped damage. Thus, while the human tragedies should not be underplayed, the fact of the matter is that the actual economic damage from the tsunami for Indonesia's economy as a whole was very small.

Nevertheless, FDI is expected to disproportionately favour China and India with the recovery of FDI into Indonesia only partially mitigating this continuing trend.

Is Southeast Asia Able to Adjust to These Challenges?

Many observers have felt that Southeast Asia will suffer heavily as a result of intensified competition from China and India — not only do these two economies have a significant cost advantage over Southeast Asia but their much larger domestic market and their impressive pools of scientists and engineers would also provide them with a competitive edge in higher value activities which Southeast Asia might attempt to upgrade to.

Such views might be too pessimistic. As Table 4 shows, most companies in Singapore and Malaysia are reasonably confident of being able to deal with intensifying competition from the two Asian giants. It is Indonesia and the Philippines

TABLE 4
Southeast Asia confident about competing with China and India

Country	Percentage of respondents agreeing with the view "We can compete with China and India"
Japan	90
Korea	83
Singapore	82
Hong Kong	79
Malaysia	78
Taiwan	77
Indonesia	43
Philippines	38

Source: Survey by Synovate and NFO World Group reported in *Business Times* (Singapore), 10 Dec 2004.
Note: Data for Thai responses not given.

— both countries that have suffered from political crises in recent years — which were less confident.

Adjustments are Underway

The main reason for our confidence that Southeast Asia can cope with the rise of China and India is that there appear to be policy responses at the macroeconomic level as well as companies responding at the microeconomic level to these growing challenges.

Domestic Policy Changes Target Removing Obstacles to Smoother Adjustment

Three sets of countries can be discerned in terms of policy responses to the Asian financial crisis: the relatively better-governed crisis-hit countries of Thailand and Malaysia have moved beyond crisis management to longer-term policy measures targeted at strengthening competitiveness and sustainability. In Thailand, the government of Premier Thaksin Shinawatra has embarked on bold policies to encourage domestic entrepreneurship, achieve greater balance in economic development between urban and rural areas and continue to attract FDI. Similarly, Malaysia is working hard to improve domestic efficiency by forcing the pace of corporate reforms in government-linked companies and by reducing protectionism in some sectors. The government has also introduced policies to grow Malaysia's emerging role as a regional education and health care centre.

Countries less affected by the Asian financial crisis are also responding with increasing resolve. In both Singapore and Vietnam, substantial policy adjustments are underway. Singapore had realized the need for change even before the Asian financial crisis hit it. Since then, it has undertaken sweeping tax reforms and liberalized key sectors such as banking, telecommunications, professional services and the media. The government has also invested heavily in emerging technologies such as biotechnology while successfully attracting global-scale investments in high-end electronics, pharmaceuticals and process chemicals.

But a third group of countries is so saddled with such a heavy burden of political dislocation or such formidable structural weaknesses, that their ability to adjust quickly was impaired, at least until recently. This includes Indonesia and the Philippines. Both Indonesia and the Philippines suffered major political and economic crises in recent years. Indonesia endured the collapse of its currency and banks in 1997, followed by a sharp economic contraction and the ouster of President Soeharto in 1998. The years since have seen a succession of political and economic shocks. It is only in the past two years that the country began to stabilize. With an impressive new administration now in place, Indonesia appears to be now in a position to look beyond the crises and focus on longer-term issues. Thus, its capacity to adjust to the growing competition from China and India is likely to improve.

The Philippines too appears to be coming out of a period of great political uncertainty that included the 2001 ouster of President Estrada in a People's Power coup, which was followed by threats of military and popular unrest. With President Arroyo having won a convincing electoral mandate and the economy performing ahead of expectations, the Philippines too might now be better-placed to undertake longer-term reforms to improve its competitiveness.

Regional Free Trade Agreements

Southeast Asian countries now realize that greater economic integration within the region and stepped up economic ties with other major trading partners will be one means of competing more effectively against China and India. With integration, the Southeast Asian economies can enjoy greater economies of scale and offer investors a larger, more unified, domestic market. Recent months have seen a flurry of new efforts to expand trade and other areas of integration:

- *Regional Initiatives*. ASEAN, the Association of Southeast Asian Nations, is also pursuing greater integration now that the ASEAN Free Trade Area has gained momentum. ASEAN wants to achieve an ASEAN Economic Community by 2020, with 11 industries selected as priority areas for accelerated integration.

- *Bilateral Free Trade Agreements*. Singapore has concluded agreements with New Zealand, Japan, the European Free Trade Area, the United States and Australia. It has also completed negotiations with South Korea and is close to concluding talks with India over similar free trade agreements. As a result of Singapore's success, others are now keen to pursue such bilateral integration initiatives as well — Thailand in particular.
- *ASEAN FTAs with Large Trading Partners*. There are also multilateral trade talks for Southeast Asia to achieve greater economic integration with Northeast and South Asia. China and ASEAN have settled on a framework for a free trade agreement while ASEAN will soon start similar talks with Japan, Korea and India. The United States has also responded with its Enterprise for Asia Initiative under which it has indicated it would favourably consider FTAs with Asian countries.

While ASEAN integration has not been as fast as many have hoped, it has nevertheless made enough progress to produce material economic benefit. For instance, the lowering of tariffs has helped ASEAN-based producers to lower costs by sourcing components from lowest-cost locations. As a result of this improved cost efficiency, there is anecdotal evidence to suggest that, say in motorcycle assembly, ASEAN-based producers have succeeded in mitigating the adverse effect of a surge in Chinese exports. Also, lower barriers to intra-ASEAN trade have enabled producers of consumer goods to consolidate production in one or two locations and thereby enjoy economies of scale they could not enjoy before.

Corporate Restructuring by Domestic Companies Boosts Competitiveness

Corporate restructuring is still a work-in-progress in Southeast Asia. Aggregate data measuring its impact is still unavailable. However, corporate actions in recent years suggests that many companies are working hard to improve their competitiveness. For instance, in Singapore, major companies have been restructuring in order to increase shareholder value. They are focusing on a narrower range of products, relocating lower-value production to cheaper locations, adopting new technologies and extracting more revenue from existing assets. This has been evident, in particular, in the largest companies in Singapore, in particular the government-linked companies. Another response has been mergers and acquisitions to gain economies of scale. This has been evident in the banking sectors in Singapore, Thailand and Malaysia, for instance.

ASEAN Economies Consequently Maintaining Competitive Position

As a result of restructuring and policy changes, ASEAN economies appear to be holding their own in terms of competitiveness. Examples from recent studies on Thailand (Table 5) and Indonesia (Table 6) lend support to this. Thailand has demonstrated a capacity to build competitive advantage in new areas; Table 5 shows new products in which Thailand has developed competitive positioning in recent years. These span a range of processed agricultural as well as manufactured goods as varied as motor vehicles and plastic materials.

Despite all the turmoil it has suffered, it is noteworthy that Indonesia too has managed to maintain some degree of export competitiveness. Note that this applies even in areas such as apparel and clothing where China's competitive advantage is said to be strong.

Chinese and Indian Demand Boosting Southeast Asia

Southeast Asia has benefited in many ways from China's rapid growth and there is increasing evidence that India's resurgent growth is also feeding through to increase demand in Southeast Asia.

TABLE 5
Thailand: Areas of increasing or strong competitive advantage

Improving Competitiveness	New products with strong competitive edge	Declining but still strong competitiveness
Animal feedstuff	Dried fruit	Fresh meat/fish
Food preparations	Natural abrasives	Vegetables
Jute/other fibre	Non-alcoholic beverages	Crude rubber
Leather	Plastic materials	Toys
Rubber articles	Rubber materials	Sound recorders
Textile yarn/thread	Non-electrical wire products	Watches/clocks
Cotton fabrics	Non-metallic mineral manufactures	Footwear
Pottery	Metal tanks	Pearls
Base metal household equipment	Road vehicles	Tin
Office machines		Lace
Electrical power machinery		Leather manufactures
Telecommunications equipment		Silk
Domestic electrical equipment		Stone
Other electrical machinery		Spices

Source: Prema-Chandra Athukorala and Suphat Suphachalasai, *ASEAN Economic Bulletin* 21, no. 1 (April 2004): 19–36.

TABLE 6
Indonesia: World Bank assessment of export competitiveness

Product	1995	2001
Coffee, tea, etc	4.3	4.1
Tobacco	0.9	1.5
Crude rubber	15.9	8.9
Pulp/waste paper	2.0	3.2
Metalliferous ores/metal scrap	4.6	4.8
Coal/etc	5.2	7.0
Petroleum/products	3.1	1.9
Gas	15.8	8.0
Fixed vegetable oils/fats	5.6	9.7
Fertilisers	2.0	0.9
Cork/wood manufactures (ex-furniture)	16.7	9.5
Telecommunications/sound recording equipment	1.0	1.3
Furniture	1.9	2.3
Travel goods/handbags	0.9	1.6
Apparel/Clothing	2.4	2.7
Footwear	6.2	4.3
Out of 63 2-digit SITC products		
No. of products with RCA > 1	17	21
% of products with RCA >1	27	33

Source: World Bank Brief for Consultative Group Indonesia Jan 2004, based on UNCOMTRADE data.
Note: RCA = revealed comparative advantage. RCA > 1 implies that country has comparative advantage in that product.

We have already seen in Figure 5 how Chinese demand has led to a substantial expansion of regional exports to China. Table 7 shows how individual countries have performed — essentially China has increased imports across the board and is set to expand on this when its FTA with ASEAN kicks in and as its demand for commodities and industrial components expands.

Clearly, if China needs to import components from Southeast Asia, that means that Southeast Asians currently possess many areas of competitive advantage; otherwise Chinese demand would have been satisfied by domestic producers.

Tourism — China and India have Rising Impact

Inflows of Chinese and Indian tourists have become progressively more important to Southeast Asia. Table 8 shows how dramatic the impact of Chinese tourism has been in Southeast Asia.

Indian tourism does not appear to have risen as much as Chinese tourism. However, despite their smaller numbers, they have had a disproportionate impact because of their substantially higher spending per head. For instance, in 2003

TABLE 7
Growth of Southeast Asian exports to China

Country	Growth in Exports to China (%) Oct '98 to Oct '04
Indonesia	126.3
Malaysia	297.3
Philippines	686.2
Singapore	319.6
Thailand	393.4

Source: Collated by Centennial Group from CEIC Data.

TABLE 8
Growing importance of Chinese and Indian tourists to Southeast Asian countries

Country	China		India	
% share of Chinese and Indian tourists/total tourists arrivals	1990	2003	1990	2003
Malaysia	0.1	3.3	0.5	1.8
Singapore	negligible	9.3	4.1	5.0
Thailand	1.1	6.2	2.4	2.3

Source: Calculated from CEIC Data.
Note: Data for Indonesia and Philippines not available.

Singapore received 309,423 Indian tourists compared to 568,449 from China but Indian tourists were estimated to have spent S$409.5m compared to S$269.9m by Chinese tourists.

Conclusion

This survey of the impact of the increased economic clout of China and India on Southeast Asia veers towards a more optimistic view of how Southeast Asia will be impacted. Southeast Asia has actually coped quite well in terms of market share of global merchandise exports. Moreover, Southeast Asian economies have expanded their exports to China rapidly while also enjoying the spillovers of growing Chinese and Indian prosperity through, for example, attracting tourists from both the Asian giants. The challenges are real and in some ways will intensify as China continues to draw substantial FDI and as India's manufacturing sector becomes much more competitive in exports as well as in competing with Southeast Asia for FDI. But Southeast Asia will not sit still: Southeast Asian policy-makers are changing policies

to cope with the increased competition while Southeast Asian companies are also likely to reinvent themselves so as to be able to find their own niches in which they can prosper.

Note

This chapter focuses mostly on the core Southeast Asian economies of Indonesia, Malaysia, Philippines, Singapore and Thailand due to the lack of data on the other Southeast Asian economies. However, wherever possible every effort has been made to indicate how the other Southeast Asian economies have been impacted.